In the Supreme Court of Missouri

No. 84415

IN THE MATTER OF THE LIQUIDATION OF PROFESSIONAL MEDICAL INSURANCE CO. and PROFESSIONAL MUTUAL INSURANCE CO. RISK RETENTION GROUP:

ARNOLD J. WOLF, D.P.M., ARTHUR AXELBANK, M.D., and JONATHAN E. KLEIN, M.D.,

Appellants,

v.

A.W. MCPHERSON, DEPUTY DIRECTOR, MISSOURI DEPARTMENT OF INSURANCE,

Respondent.

Appeal from the Circuit Court of Jackson County, Missouri
Honorable Lee E. Wells, Judge

REPLY BRIEF OF APPELLANTS

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REPLY TO RESPONDENT'S STATEMENT OF FACTS

Respondent states at page 6 of his Statement of Facts, that following his February 4, 1999, memorandum to the court, Judge Wells elected not to "appoint a trustee to investigate claims ProMed might have had against RRG or claims RRG might have had against ProMed," thereby suggesting that the existence of such claims was revealed to the Court. That is not the case.

While the February 4, 1999, memorandum does contain a transactional history of sorts, it does not disclose the existence of claims or potential claims between the two estates; it does not opine on the validity or strength of any such claims; it does not reveal the reasons for electing not to pursue any such claims; nor does it contain any mention of the fact that the Receiver had a clear conflict of interest in all three areas. That is, Respondent did not report that any disclosure or identification of such claims, any evaluation of the merits of such claims and any decision not to pursue such claims necessarily created a conflict of interest for the Receiver.

By arguing that Judge Wells should have been able to infer from the February 4, 1999, memorandum that the Receiver had a clear conflict of interest, the Receiver betrays his own knowledge of that fact on February 4, 1999 and thus his own flagrant violation of ***R.S.Mo. § 375.710*** which mandates the disclosure of such conflict of interest to the Court.

Similarly, the Receiver's suggestion at p. 6 that in November 1999 the trial court elected no to appoint a trustee for RRG, is unsupported by the record which reveals that the issue of conflict of interest was not addressed by Judge Wells in any fashion until the December 20, 2000, hearing at which time he expressly refused to consider the issue.

REPLY TO RESPONDENT'S ARGUMENT

In the introductory paragraph of Respondent's Argument section, the Receiver again misstates the record with respect to the conflict of interest issue when he states that "with full knowledge of the underlying facts and mindful of the remedies provided in Mo.Rev. Stat. §375.710" the trial court addressed the conflict of interest issue. Again, the record reflects that the issue of conflict of interest was not raised until the Receiver admitted the existence of a conflict of interest in the October 30, 2000, hearing. *See* Substitute Brief of Appellants, p. 12. The Receiver now argues that the conflict of interest he conceded on October 30, 2000, may not exist – "if indeed there was a conflict." *See* Substitute Brief of Respondent, p. 12.

The trial court did not in any way address the conflict of interest issue until the December 20, 2000, hearing when he refused to address the matter. *See* Substitute Brief of Appellants, p. 13. The Receiver now argues that the trial court's refusal to examine whether there was a conflict of interest amounts to the "mak[ing] such other orders" under ***R.S.Mo. § 375.710*** as are required once a determination has been made that a conflict of interest exists.

I. THE TRIAL COURT ERRED IN DENYING APPELLANTS' MOTION TO INTERVENE BECAUSE APPELLANTS ESTABLISHED THE NECESSARY ELEMENTS UNDER RULE 52.12 TO BE ENTITLED TO INTERVENE AS A MATTER OF RIGHT SUCH THAT THE TRIAL COURT'S DENIAL CONSTITUTED AN ERRONEOUS APPLICATION OF THE LAW.

It is noteworthy, as an initial matter, that the Receiver concedes he did not at any time object in the trial court to Appellants' motions to intervene. *See* Substitute Brief of Respondent, p. 13. That fact alone should cause this Court to view with skepticism the trial court's denial of appellants' motions to intervene.

The Receiver first argues that receivership proceedings in general are not considered actions for purposes of ***Rule 52.12(a)***, such that appellants could have no right to intervene. This argument assumes – and indeed the Receiver specifically states – "appellants sought to intervene in the ProMed receivership estate generally, for all purposes." *See* Substitute Brief of Respondent, p. 14. However, that is simply not the case.

While Appellant Wolf's original motion to intervene might have been so interpreted,[1] the supplemental motion for leave to intervene accompanied by a petition

[1] The initial motion for leave to intervene was patterned after the motion filed by the ESOP participants that had been previously granted by the trial court. Appellant Wolf, at the time the initial petition was filed, did not have access to sufficient information upon which to base a petition in

[L.F. 26-37], made it clear that Appellants were seeking intervention only for the purpose of asserting the derivative actions described in the petition. Appellants did not seek to intervene "generally" or "for all purposes" and, therefore, the denial of appellants' motion for leave to intervene cannot be justified based on the holding of ***Ainsworth v. Old Security Life Insurance Company,*** 685 S.W.2d 583, 585 (Mo. App. 1985) (***Ainsworth I***). Appellants agree with the ***Ainsworth I*** court that and applicant "asks too much when it asks to be made a part of the receivership itself." ***Id.*** at 586.

The ***Ainsworth I*** court, however, also made it clear that intervention in a *particular proceeding* in which the Receiver may be involved, is not only *permissible* but should be "*allowed with considerable liberality*." ***Id.*** at 585. (Emphasis added).

The Receiver next argues that the non-existence of a "pending, ancillary action" at the time Appellants sought to intervene is fatal to Appellants' right to intervene. *See* Substitute Brief of Respondent, p. 15. The Receiver again misinterprets the holding in ***Ainsworth I***. The issue is not whether the ancillary action *exists* at the time intervention is sought or whether the ancillary action would be *created by* the intervention, the issue is the scope of the intervention sought. ***Ainsworth I*** makes it clear that plenary

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intervention.

intervention is impermissible because "[i]t would too much encumber the receivership proceeding." ***Id.*** at 586. At the same time, ***Ainsworth I*** clearly announces that intervention in "particular proceedings" should be "allowed with considerable liberality." ***Id.*** Were the Court to do as the Receiver suggests and require that there be a "pending, ancillary action" before intervention for a particular proceeding can be allowed, there would be no mechanism by which a Receiver's refusal to pursue claims owned by the Receivership estate could ever be challenged or remedied. As pointed out in the Substitute Brief of Appellants (p. 23), the court supervising the liquidation of the insurance company has exclusive subject matter jurisdiction to hear claims against the receiver. ***Medallion Insurance Company v. Wartenbee,*** 568 S.W.2d 599, 601 (Mo. App. 1978). Denial of intervention to those seeking to challenge a Receiver's failure to pursue receivership claims on the grounds that there is no "pending, ancillary action" into which to intervene, would create a "Catch-22," the effect of which would be to immunize the Receiver from any challenge to his refusal to pursue such claims. There is no policy justification for such a result and it is at odds with the rule that limited intervention for purposes of "particular proceedings" should be "allowed with considerable liberality."

The Receiver's third argument under this Point is that Appellants failed to perfect any claim they may have had by filing a claims in the ProMed estate. *See* Substitute Brief of Respondent, p. 16. This argument either misstates or misunderstands the nature of the claim that Appellants sought to pursue. Appellants, individually, had no right or

standing to file a claim in the ProMed estate. Appellants were never shareholders of ProMed. Rather, RRG was the shareholder of ProMed and, consequently, it was RRG itself – more particularly, the Receiver of RRG – who was obligated to file a claim against ProMed. The RRG Receiver refused to do so.

It was upon learning of the existence of , and because of the RRG Receiver's refusal to pursue RRG's claim against ProMed, that Appellants sought to intervene to pursue that action derivatively. Indeed, one of the essential elements of a derivative action is that the management of the entity refuses to take remedial action. ***Goodwin v. Goodwin***, 583 S.W.2d 559, (Mo. App. E.D. 1979). In this case, the only remedial action available to appellants was to assert RRG's claim to the ownership of the ProMed stock against ProMed and stockholders, by means of a derivative action against the RRG Receiver himself.

The Receiver argues in essence that his own failure to assert RRG's claim against ProMed itself insulates him from a derivative claim seeking to force him to assert that claim. In effect, the Receiver is asserting that he ought to be able to take whatever action it wants – even if tainted by an admitted but undisclosed conflict of interest – and then assert his own action or inaction as an absolute bar to anyone seeking to have his actions reviewed.

II. THE TRIAL COURT ERRED WHEN IT REFUSED TO EVEN CONSIDER THE QUESTION OF THE RECEIVER'S CONFLICT OF INTEREST BECAUSE THE RECEIVER ADMITTED THE

EXISTENCE OF THE CONFLICT OF INTEREST AND R.S.MO. § 375.710 GIVES THE TRIAL COURT NO DISCRETION TO REFUSE TO EXAMINE THE ISSUE OF A RECEIVER'S CONFLICT ONCE A CONFLICT OF INTEREST IS REPORTED.

In response to Appellants' point that the trial court erred in failing to address the Receiver's conflict of interest, the Receiver makes essentially three arguments.

First, the Receiver argues that his February 4, 1999 memorandum "gave the trial court several different options" including those set forth in ***R.S.Mo. § 375.710,*** which are available to a trial court who has had a conflict of interest disclosed to him. Contrary to Receiver's argument, neither the existence of a conflict of interest, nor the responses available under ***§375.710***, are disclosed in the February 4, 1999 memorandum. In fact, the Receiver's very next argument is his suggestion that there really was no conflict of interest. *See* Substitute Brief of Respondent, p. 19. Receiver is only able to make the second argument by reason of his failure to comply with his mandatory disclosure obligations under ***R.S.Mo. § 375.710*** , which makes it the "duty of the [Receiver] . . . ***to report the fact of conflict and the question or questions involved to the court in which any of the cause is pending***. (Emphasis added).

Obviously, had the Receiver reported the ***fact*** of a conflict of interest to the trial court as he was obligated by ***§375.710*** to do, he could not now be heard to argue that there was really no such conflict of interest. Only the breach of the Receiver's statutorily

mandated duty of disclosure permits him the present convenience of simultaneously arguing that he disclosed the conflict of interest and that there was no conflict of interest to disclose.

The Receiver argues presently that the Receiver had no conflict of interest because the claim at issue is now barred because the Receiver failed to timely assert it. *See* Substitute Brief of Respondent, pp. 18-19. To accept this question begging argument from Respondent is to eviscerate the safeguards contained in ***R.S.Mo. § 375.710.*** The RRG Receiver is the one charged in the first instance with asserting, or choosing not to assert, any claims owned by RRG. Where the decision not to assert a claim may be tainted by conflict of interest, justice demands that the disclosure of the conflict of interest be made before the claim is irrevocably lost to a time bar. However, the Receiver admits the first time it even arguably disclosed the conflict of interest was in the February 4, 1999, memorandum, after the claim had become time-barred. The Receiver now in essence argues that because he allowed the bar date to pass without disclosing the conflict or asserting the claim, the conflict of interest ceased to exist.

The Receiver's final argument is simply a repetition of the argument that Judge Wells refusal to even consider the question of whether there was a conflict of interest is the functional equivalent of finding the existence of a conflict of interest and applying the remedial provisions of ***R.S.Mo. § 375.710.*** This argument has already addressed. However, it bears mentioning that all parties seemingly agree that Judge Wells' refusal to

take action was due largely to his stated desire to close the estate. Presumably, that concern would not have held sway had the Receiver disclosed the conflict of interest to Judge Wells earlier in the life of the Receivership. In other words, even the Court assumes – contrary to Judge Wells' express statements – that Judge Wells believed in December 2000 that he was applying the remedial provisions of ***§375.710***, the prejudice to appellants by reason of the RRG Receiver's failure to earlier disclose the conflict of interest still looms large.

REPLY TO STATEMENT OF FACTS OF

AMICI CURIAE CIC, INC. AND JOURDON

Jourdon and CIC ask the Court, without support of any authority, to discount or ignore the facts contained in appellants' Statement of Facts because the facts are in an unsigned petition in intervention. *See* Brief of Amici CIC/Jourdon, p. 6. However, the law is clear that when a motion is at issue on appeal, all well-pled facts contained in the motion will be taken as true. ***Missouri Municipal League v. Brunner,*** 740 S.W.2d 957, 958 (Mo. 1987).

In contrast, the "facts" set forth by CIC/Jourdon are not contained in the motion, nor in many cases, supported by the record. For the most part, they consist of argument that attempts to suggest that Jourdon "earned" the millions of dollars he received for the stock of ProMed for which he paid nothing. It is these facts that the Court must ignore.

REPLY TO THE ARGUMENT

OF AMICI CIC/JOURDON

1. THE TRIAL COURT ERRED IN DENYING APPELLANTS' MOTIONS FOR LEAVE TO INTERVENE BECAUSE APPELLANTS ESTABLISHED THAT THEY MET THE NECESSARY ELEMENTS OF RULE 52.12(a) AND SUCH RULE APPLIES WITH EQUAL FORCE TO ANCILLARY PROCEEDINGS WITHIN A RECEIVERSHIP.

Amici argue that Appellants have no right to intervene under Amici's interpretation of the Insolvency Code. Amici attempt to distinguish ***Ainsworth I*** and ***Ainsworth v. Old Security Life Insurance Company***, 694 S.W. 2d 838 (Mo. App. W.D. 1985) **(*Ainsworth II*)**, both of which state that such intervention is not only permissible, but to be allowed with "considerable liberality." Amici otherwise cite no case law for their argument that the Insolvency Code does not permit intervention. Amici's failure to cite authority merely makes Amici's argument weak. What reduces it to the realm of the frivolous is the fact that *Amici asked for and were allowed intervention into these very receiverships* in order to challenge the refusal of ProMed's Receiver to make claims Amici thought should have been asserted against RRG. *See* Appendix to Substitute Brief of Appellants. Needless to say, Amici did not then take the position that they had no right under the Insolvency Code to intervene. By intervening they delayed any distribution from the RRG estate during the pendency of that intervention. Amici's argument should therefore be rejected.

Without any factual basis for doing so, Amici argues contrary to the record that "appellants allowed years to pass" without seeking intervention. The record is clear that appellants only learned of the facts supporting their claim in September 1999 when Amici attempted to fraudulently purchase assignments of

their interests in RRG. (Transcript of December 20, 2000, hearing, p. 14). That fraudulent effort on the part of Amici resulted in the Receiver seeking and obtaining a temporary restraining order from Judge Wells. (L.F. 9-13). Thus, appellant Wolf attempted immediately to intervene. Amici's assertion that appellants "allowed years to pass" without attempting to intervene is therefore completely unfounded. *See* Brief of Amici CIC/Jourdon, p. 15.

II. THE TRIAL COURT ERRED IN REFUSING TO ADDRESS APPELLANTS' REPORT OF A CONFLICT OF INTEREST ON THE PART OF THE RECEIVER BECAUSE THE RECEIVER ADMITTED THE EXISTENCE OF THE CONFLICT AND ADMITTED THAT THE RECEIVER HAD NOT DONE EVERYTHING HE COULD TO PROTECT RRG'S INTEREST, THUS MANDATING APPLICATION OF THE REMEDIAL PROVISIONS OF R.S.MO. § 375.710.

After repeating their unsupported argument that appellants allowed years to pass without attempting to intervene, Amici next assert that Appellants have no right to raise the issue of conflict of interest because Appellants did not present evidence of a conflict of interest. Amici assert that the trial court "concluded no conflict of interest was present" despite the clear record that the trial court refused to even address the issue. *See* Substitute Brief of Appellants, p. 13.

Amici's final argument on this Point seeks to reduce the conflict of interest analysis to the undefined term "favoritism" which it then argues was not present. Amici appear to be arguing that because the Receiver placed the company in receivership to begin with and made some decisions with which they did not agree, *ipso facto*, the Receiver cannot have conflict of interest. Such an argument is self-evidently untenable. Clearly, the mere existence of substantial claims by one receivership estate against the other give rise to a conflict of interest on the part of the Receiver. There is no requirement that every single decision

made by the receiver must work to the disadvantage of appellants.

III. BY FAILING TO SEEK INTERVENTION TO CHALLENGE THE ASSIGNMENT BY THE RRG RECEIVER, AMICI HAVE NO STANDING TO ASK THIS COURT TO REFRAIN FROM ADDRESSING AN ISSUE INEXTRICABLY BOUND UP IN THIS APPEAL.

In its third point Amici seek to mislead the Court into declaring that the trial court has not approved of the assignment given by the Receiver to Appellants. The fact is that the trial court did approve that assignment and Amici have taken no appeal therefrom. It is also clear from the record that the trial judge's denial of Appellants' motion for leave to intervene was based at least in part on the trial court's belief that viable claims could be pursued by Appellants via assignment outside of the Receivership estate. If, as Amici assert, the assignment is invalid, this bears upon the correctness of the trial court's refusal to grant intervention. By arguing that the denial of intervention should be affirmed without discussion of the validity of the assignment, Amici seek once again to have their cake and eat it too. That is, they seek to benefit from the denial of intervention — which was based on the trial court's belief the claims could adequately be pursued outside the Receivership estate — yet reserve the right to later claim the assignment was invalid. Amici thereby hope to avoid any inquiry into their fraudulent activities, which inquiry the trial judge has already characterized as "legitimate claims."

Appellants do not believe the assignments grant to them all of what they need to enforce their claims against Jourdon/CIC and others. For example, the assignment does not appear to give Appellants any right to delay the distribution of the approximately $5 million remaining in ProMed to Jourdon/CIC and the ESOP during the pendency of an action outside the receivership proceeding, while the granting of Appellants' motion for leave to intervene would protect those funds within the estate. However, the issue

of whether the Receiver has the authority to make such an assignment is before the Court at least indirectly if not directly. The Court should decline the invitation of Amici to declare otherwise.

REPLY TO ARGUMENT OF AMICI

CERTAIN ESOP PARTICIPANTS

I. THE TRIAL COURT ERRED IN DENYING APPELLANTS' MOTION TO INTERVENE BECAUSE APPELLANTS ESTABLISHED THE NECESSARY ELEMENTS UNDER RULE 52.12 TO BE ENTITLED TO INTERVENE AS A MATTER OF RIGHT SUCH THAT THE TRIAL COURT'S DENIAL CONSTITUTED AN ERRONEOUS APPLICATION OF THE LAW.

In support of their argument that appellants have no interest under ***Rule 52.12(a),*** Amici ESOP participants cite ***State ex rel. Missouri State Life Insurance Company,*** 52 S.W.2d 174, 330 Mo. 1107 (1932) and ***State ex rel. St. Louis Mutual Life Insurance Company v. Mulloy,*** 52 S.W.2d 469, 330 Mo. 951 (1932). In both cases, the trial judges attempted to in essence set up receiverships by appointing someone outside of the Department of Insurance as receivers. These cases shed no light on the question of whether a party has a right to intervene in a receivership created under the Insurance Code. That is the question addressed by ***Ainsworth I*** and ***Ainsworth II***, both of which hold that such intervention for a limited purpose should be allowed with "considerable liberality."

Curiously, after suggesting that these two cases from 1932 are of continued vitality, Amici ESOP participants seem to suggest that changes to the insurance code after the two ***Ainsworth*** decisions somehow compromises their vitality. Nothing in the

additional statutory sections enacted after the two ***Ainsworth*** decisions undercuts their authority.

Amici ESOP participants next argue that a constructive trust is not allowed under the Insurance Code. This issue is not before the Court in any way. The issue is whether appellants have an interest supporting intervention of right. The scope and form of the remedies are not at issue.

II. THE TRIAL COURT ERRED WHEN IT REFUSED TO EVEN CONSIDER THE QUESTION OF THE RECEIVER'S CONFLICT OF INTEREST BECAUSE THE RECEIVER ADMITTED THE EXISTENCE OF THE CONFLICT OF INTEREST AND R.S.MO. § 375.710 GIVES THE TRIAL COURT NO DISCRETION TO REFUSE TO EXAMINE THE ISSUE OF A RECEIVER'S CONFLICT ONCE A CONFLICT OF INTEREST IS REPORTED.

Amici ESOP participants' entire argument with respect to the conflict of interest point depends upon their assertion that appellants failed to file proofs of claim. As has been pointed out above, the claim belonged to the RRG Receiver, not appellants directly. Appellants were never in a position to file a claim in the ProMed estate because none of them, individually, ever owned any of the stock in ProMed. Rather, the claim against ProMed was vested in the RRG Receiver who, without disclosing the claim, his reason for not asserting it and his conflict of interest, simply chose not to assert it. This failure must be remedied by this Court or by the trial court upon remand.

CONCLUSION

Whether it be through the intervention of right provisions of ***Rule 52.12(a)*** or the conflict of interest provisions of ***R.S.Mo. § 375.710***, there has to be some remedy when policyholders of a mutual company such as appellants learn that the Deputy Director of the Missouri Department of Insurance who owes them fiduciary obligations has knowingly looked the other way while one of his former colleagues either has pocketed or will pocket between twenty and thirty million of dollars that rightfully belong to their company.

Additionally, in the words of the trial judge, RRG has "legitimate claims" arising out of the transaction whereby it lost its 100% ownership interest in ProMed. Appellants established that they met all the elements of ***Rule 52.12(a)*** and simultaneously demonstrated that the Receiver had an impermissible conflict in "decid[ing] the stock resides where it does" and electing not to pursue those claims against ProMed. Under these facts, the court was required to grant Appellants leave to intervene and/or appoint trustees to pursue the action against ProMed and Jourdon/CIC. The one thing the trial court could not do is precisely what it did — ignore the conflict of interest and hurriedly distribute the money under the mistaken belief that it would "expedite the closing" of the Receiverships estates.

This Court should take this opportunity to address flagrant abuses by the Missouri Department of Insurance and its supervised receiverships.

This Court should also reverse the trial court's Order and remand this case with

directions to the trial court to grant Appellants' Motion for Leave to Intervene and/or appoint one or more Receivers to pursue the claims of RRG.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that:

1. The brief includes the information required by Supreme Court Rule 55.03;

2. The brief complies with the limitations contained in Supreme Court Rule 84.06(b); and

3. According to the Word Count Function of counsel's word processing software, the brief contains _____ words.

_____
Martin M. Meyers